

Internal Revenue Service, Treasury

§ 1.817-2

§ 1.815-2 for any taxable year shall be adjusted to the extent necessary to properly reflect a subsequent loss from operations which under section 812 is carried back to the taxable year for which such additions or subtractions were made.

(2) *Example.* The application of subparagraph (1) of this paragraph may be illustrated by the following example:

Example. Assume that for the taxable years 1959 through 1961, the books of S, a stock life insurance company subject to a 30 percent tax rate for all taxable years involved, reflect the following items:

	1959	1960	1961
Taxable investment income	\$40.00	\$40.00	\$40.00
Gain from operations	60.00	60.00	60.00
Tax base (sec. 802(b)(1) and (2))	50.00	50.00	50.00
Tax (sec. 802(b)(1) and (2) base)	15.00	15.00	15.00
Shareholders surplus account—			
At beginning of year ...	0	35.00	37.00
Added at beginning of year by reason of election under sec. 815(d)(1)	0	7.00	0
Added for year (without regard to election under sec. 815(d)(1))	35.00	35.00	35.00
Subtracted (distributions)	0	40.00	40.00
Policyholders surplus account—			
At beginning of year ...	0	0	10.00
Added for year	10.00	10.00	10.00
Subtracted (distributions)	0	0	0
Subtracted (by reason of election under sec. 815(d)(1))	10.00	0	0
Tax base (sec. 802(b)(3))	10.00	0	0
Tax (sec. 802(b)(3) base)	3.00	0	0

Assume further that S has a loss from operations for the taxable year 1962 of \$25. Under the provisions of section 812, the \$25 loss from operations would be carried back to the taxable year 1959 and would reduce the 1959 tax base under section 802(b)(1) and (2) to \$35 (\$60 minus \$25). After adjustments reflecting the 1962 loss from operations, the results for the taxable years 1959 through the beginning of 1962 would be as follows:

	1959	1960	1961	1962
Taxable investment income	\$40.00	\$40.00	\$40.00	.....
Gain from operations	35.00	60.00	60.00	.....
Tax base (sec. 802(b)(1) and (2)) ...	35.00	50.00	50.00	.....

	1959	1960	1961	1962
Tax (sec. 802(b)(1) and (2) base)	10.50	15.00	15.00	.....
Shareholders surplus account—				
At beginning of year	0	24.50	19.50	\$14.50
Added for year (without regard to election under sec. 815(d)(1))	24.50	35.00	35.00	.....
Added by reason of election under sec. 815(d)(1)	0	0	0	.....
Subtracted (distributions)	0	40.00	40.00	.....
Policyholders surplus account—				
At beginning of year	0	0	10.00	20.00
Added for year	0	10.00	10.00	.....
Subtracted (distributions)	0	0	0	.....
Subtracted (by reason of election under sec. 815(d)(1))	0	0	0	.....
Tax base (sec. 802(b)(3))	0	0	0	.....
Tax (sec. 802(b)(3) base)	0	0	0	.....

As a result of the loss from operations for 1962, the election under section 815(d)(1) for the taxable year 1959 has become inapplicable in its entirety since the balance in the policyholders surplus account at the end of 1959, as recomputed, is zero. Thus, S would be entitled to a total refund of \$7.50 for the taxable year 1959. Of this amount, \$4.50 is due to the recomputation of the section 802(b)(1) and (2) tax base and \$3 to the amount of tax paid by reason of the election under section 815(d)(1).

[T.D. 6535, 26 FR 545, Jan. 20, 1961]

MISCELLANEOUS PROVISIONS

§ 1.817-1 Taxable years affected.

Except as otherwise provided therein, §§ 1.817-2 through 1.817-4 are applicable only to taxable years beginning after December 31, 1957, and all references to sections of part I, subchapter L, chapter 1 of the Code are to the Internal Revenue Code of 1954, as amended by the Life Insurance Company Income Tax Act of 1959 (73 Stat. 112) and section 3 of the Act of October 23, 1962 (76 Stat. 1134).

[T.D. 6886, 31 FR 8689, June 23, 1966]

§ 1.817-2 Treatment of capital gains and losses.

(a) *In general.* For taxable years beginning after December 31, 1958, and before January 1, 1962, if the net long-

term capital gain (as defined in section 1222(7)) of any life insurance company exceeds its net short-term capital loss (as defined in section 1222(6)), section 802(a)(2) prior to its amendment by section 3 of the Act of October 23, 1962 (76 Stat. 1134), imposes a separate tax equal to 25 percent of such excess. For taxable years beginning after December 31, 1961, if the net long-term capital gain of any life insurance company exceeds its net short-term capital loss, section 802(a)(2) imposes an alternative tax in lieu of the tax imposed by section 802(a)(1), if and only if such alternative tax is less than the tax imposed by section 802(a)(1). Except as modified by section 817 (rules relating to certain gains and losses), the general rules of the Code relating to gains and losses, such as subchapter O (relating to gain or loss on disposition of property), subchapter P (relating to capital gains and losses), etc., shall apply with respect to life insurance companies.

(b) *Modification of section 1221 and 1231.* (1) In the case of a life insurance company, section 817(a)(1) provides that for purposes of applying section 1231(a) (relating to property used in the trade or business and involuntary conversions), the term *property used in the trade or business* shall be treated as including only:

(i) Property used in carrying on an insurance business, of a character subject to the allowance for depreciation under section 167 (even though fully depreciated), held for more than 1 year (6 months for taxable years beginning before 1977; 9 months taxable years beginning in 1977), and real property used in carrying on an insurance business, held for more than 1 year (6 months for taxable years beginning before 1977; 9 months taxable years beginning in 1977), and which is not:

(a) Property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year;

(b) Property held by the taxpayer primarily for sale to customers in the ordinary course of business; or

(c) A copyright, a literary, musical, or artistic composition, a letter or memorandum, or similar property held by a taxpayer described in section 1221(3). In the case of a letter, memo-

randum, or property similar to a letter or memorandum, this subdivision (c) applies only to sales and other dispositions occurring after July 25, 1969.

(ii) The cutting or disposal of timber, or the disposal of coal or iron ore, to the extent considered arising from a sale or exchange by reason of the provisions of section 631 and the regulations thereunder.

(2) In the case of a life insurance company, section 817(a)(2) provides that for purposes of applying section 1221(2) (relating to the exclusion of certain property from the term capital asset), the reference to property used in trade or business shall be treated as including only property used in carrying on an insurance business.

(3) Section 1231(a), as modified by section 817(a)(1) and subparagraph (1) of this paragraph, shall apply to recognized gains and losses from the following:

(i) The sale, exchange, or involuntary conversion of the following property, if held for more than 1 year (6 months for taxable years beginning before 1977; 9 months taxable years beginning in 1977):

(a) The home office and branch office buildings (including land) owned and occupied by the life insurance company;

(b) Furniture and equipment owned by the life insurance company and used in the home office and branch office buildings occupied by the life insurance company; and

(c) Automobiles and other depreciable personal property used in connection with the operations conducted in the home office and branch office buildings occupied by the life insurance company.

(ii) The involuntary conversion of capital assets held for more than 1 year (6 months for taxable years beginning before 1977; 9 months taxable years beginning in 1977).

(iii) The cutting or disposal of timber, or the disposal of coal or iron ore, to the extent considered arising from a sale or exchange by reason of the provisions of section 631 and the regulations thereunder.

(4) Section 1221(2), as modified by section 817(a)(2) and subparagraph (2) of

this paragraph, shall include only the following property;

(i) The home office and branch office buildings (including land) owned and occupied by the life insurance company;

(ii) Furniture and equipment owned by the life insurance company and used in the home office and branch office buildings occupied by the life insurance company; and

(iii) Automobiles and other depreciable personal property used in connection with the operations conducted in the home office and branch office buildings occupied by the life insurance company.

(5) If an asset described in subparagraph (3) (i)(a), (b), or (c) or subparagraph (4) of this paragraph, or any portion thereof, is also an "investment asset" (an asset from which gross investment income, as defined in section 804(b), is derived), such asset, or portion thereof, shall not be treated as an asset used in carrying on an insurance business. Accordingly, the gains or losses from the sale or exchange (or considered as from the sale or exchange) of depreciable assets attributable to any trade or business, other than the insurance trade or business, carried on by the life insurance company, such as operating a radio station, housing development, or a farm, or renting various pieces of real estate shall be treated as gains or losses from the sale or exchange of a capital asset unless such asset is involuntarily converted (within the meaning of paragraph (e) of § 1.123-1).

(c) *Illustration of principles.* The provisions of section 817(a) and this section may be illustrated by the following examples:

Example 1. L, a life insurance company, has recognized gains and losses for the taxable year 1959 from the sale or involuntary conversion of the following items:

	Gains	Losses
Stocks, held for more than 6 months	\$100,000	.....
Bonds, held for more than 6 months		\$5,000
Housing development, held for more than 6 months		400,000
Branch office building owned and occupied by L, held for more than 6 months		115,000

	Gains	Losses
Furniture and equipment used in the investment department, held for more than 6 months	30,000	.....
Radio station, held for more than 6 months	200,000	.....
Involuntary conversion of apartment building, held for more than 6 months	7,000	.....

The recognized gains and losses from the sale of the stocks, bonds, housing development, and radio station shall be treated as gains and losses from the sale of capital assets since such items are capital assets within the meaning of section 1221 (as modified by section 817(a)(2)). Accordingly, the provisions of section 1231 shall not apply to the sale of such capital assets. However, the provisions of section 1231 (as modified by section 817(a)(1)) shall apply to the sale of the branch office building and the furniture and equipment, and the apartment building involuntarily converted. Since the aggregate of the recognized losses (\$115,000) exceeds the aggregate of the recognized gains (\$37,000), the gains and losses are treated as ordinary gains and losses.

Example 2. Y, a life insurance company, owns a twenty-story home office building, having an adjusted basis of \$15,000,000, ten floors of which it rents to various tenants, one floor of which is utilized by it in operating its investment department, and the remaining nine floors of which are occupied by it in carrying on its insurance business. If in 1960, Y sells the building for \$10,000,000, Y must first apportion its basis between that portion of the building (one-half) used in carrying on an insurance business, and that portion of the building (one-half) classified as an "investment asset", before it can determine the character of the loss attributable to each portion of the building. For such purpose, the one floor utilized by Y in operating its investment department is treated as used in carrying on an insurance business. Assuming that each portion of the building bears an equal (one-half) relation to the basis of the entire building, Y (without regard to section 817(b)) would have a \$2,500,000 ordinary loss on that portion used in carrying on an insurance business (assuming that Y had no gains subject to section 1231), and a \$2,500,000 capital loss on that portion of the building classified as an investment asset.

[T.D. 6558, 26 FR 2782, Apr. 4, 1961, as amended by T.D. 6841, 30 FR 9308, July 27, 1965; T.D. 6886, 31 FR 8689, June 23, 1966; T.D. 7369, 40 FR 29840, July 16, 1975; T.D. 7728, 45 FR 72650, Nov. 3, 1980]